Western Wireless Petition for Rulemaking
To Eliminate Rate-of-Return Regulation of ILECs

<u>Top Ten Reasons to Eliminate Rate-of-Return ("ROR") Regulation</u>

1. **<u>Save Money</u>.** By far the largest cause of the growth of the high-cost universal service fund is disbursements to rural ILECs pursuant to ROR formulas. Consumers across the country would save hundreds of millions, possibly billions, of dollars if ROR were eliminated and replaced with a system better targeted to support affordable service for consumers in high-cost areas.

2. **<u>Stop Waste, Fraud and Abuse</u>.** Regulators and independent auditors rarely, if ever, look at the accounting books of most ROR carriers, and opportunities abound for carriers to overstate their costs and thereby increase their access charges and high-cost support. The Supreme Court recognized that the ILECs' "book costs may be overstated by approximately $5 Billion." [*Verizon v. FCC*, 535 U.S. 467, 518 (2002)]

3. **<u>Prevent Cross-Subsidies and Cost Misallocation</u>.** In the few cases where the FCC or a state commission examined carriers cost submissions, they found millions of dollars of misallocated costs, including costs of unregulated affiliates assigned to the ILEC in order to inflate high-cost support. In most cases, the FCC may lack authority to order remedies for such over-earnings. "In an era of corporate governance problems and accounting depredations," [Adelstein/Copps statement, FCC 03-111, 5/19/03], the FCC should change the rules to eliminate the rewards for such anti-competitive misconduct.

4. **<u>Create Incentives for Efficiency</u>.** ROR regulation gives carriers incentives "to adopt the most costly, rather than the most efficient, investment strategies," [3 FCC Rcd 3195, 3219-20]. Ending ROR would create incentives for more efficient networks, and would benefit consumers.

5. **<u>Enhance Incentives for Innovation</u>.** The FCC has recognized that ROR "may have a negative effect on innovation . . . . because a carrier's reward for such innovation is a reduction in its dollar earnings." [3 FCC Rcd 3195, 3223]. Eliminating ROR regulation would enhance incentives to speed the deployment of new technologies, benefitting rural consumers.

6. **<u>Remove Barriers to Competition in Rural Areas</u>.** Rural customers benefit from access to competitive telecom alternatives, but ROR regulation is a barrier to full competition. ROR targets RLECs' revenues to achieve a guaranteed return on investment on all historical costs incurred, while the RLECs' competitors receive portable funding only if they can obtain ETC designation, and even then only with respect to the lines that they provide – and unlike the RLECs, competitive carriers' investments are at risk.

7. **<u>Fix Distorted Intercarrier Compensation</u>.** Eliminating ROR would enable the FCC to remove implicit subsidies from the RLECs' access rates, as the Act requires.The RLECs' current, unreasonably high access charges distort local and long-distance competition in rural areas, deprive rural consumers of access to long-distance alternatives, and interfere with the development of a comprehensive, rational system of intercarrier compensation.

8. **<u>Rationalize and Modernize High-Cost Support</u>.** The current high-cost support system is an irrational hodge-podge that gives rural ILECs vastly more support than larger carriers for serving

identical geographic areas, rewards them simply for being small, and ignores whether they are efficient or not. The ROR paradigm must be replaced with a competitively neutral system that ensures "sufficient funding of *customers*, not *providers*," as the 1996 Act requires. [*Alenco*, 201 F.3d 608, 620 (5th Cir. 2000).]

9. **Remedy Unhealthy Dependence of RLEC Sector.** Many RLECs receive 70% or more of their funding from universal service subsidies or intercarrier payments, rather than from their own customers. This unhealthy dependence insulates these carriers from any incentive to be responsive to their own consumers' needs. Eliminating ROR and rebalancing rates would put these carriers on a healthier financial footing.

10. **The FCC Was Correct and Should Keep Its Promises.** In the 2001 *RTF Order*, the FCC reaffirmed its 1997 commitment to adopting forward-looking cost-based support mechanisms for rural carriers. It is time for the Commission to deliver on this worthy commitment.

In sum, ROR regulation bloats the universal service fund, creates opportunities and incentives for waste, fraud and abuse, and inhibits the development of efficient, innovative, and competitive services for rural consumers. ROR regulation has outlived its time and must be replaced with a more appropriate form of regulation based upon today's competitive environment.

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Western Wireless proposes to replace ROR regulation with a forward-looking cost-based system to determine universal service high-cost support and access charge rate levels:

- **Cost Methodology.** Develop a model or other cost analysis methodology that accurately estimates the forward-looking cost of wireline service in high-cost areas. Develop a similar model or other methodology to estimate the forward-looking cost of *wireless* service. Support would be based on the lower of the wireline or wireless forward-looking cost in each geographic area.

- **Support Methodology.** Provide two types of support: the first based on a simple comparison of the cost of service with a national benchmark, and the second based on statewide averages. As an inducement to rate rebalancing and eliminating implicit subsidies in retail rates, limit support to carriers with retail rates that are below minimum "affordable" levels.

- **Phase In the New System.** Implement the new rules in 2006 (at the end of the 5-year period provided by the *RTF Order*) for competitive ETCs, non-rural ILECs, and rural ILECs owned by relatively large holding companies. Phase in the rules over the following 6 years for smaller rural ILECs.

- **Establish "Safety Net" and "Hold Harmless" Mechanisms.** To avoid rate shock, implement the plan so that no study area loses more than a specified percentage of the amount of support it previously received in any one year. Offer additional support if a carrier can prove that the forward-looking support amount is insufficient given its particular circumstances.

- **Reform Access Charges.** Rebalance access charges by moving non-traffic sensitive costs and other implicit subsidies out of access charges paid by long-distance carriers, and into subscriber line charges. Set RLEC access rates based on forward-looking costs, price cap mechanisms, and/or generic intercarrier compensation rules.

Western Wireless **News Release**

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FOR IMMEDIATE RELEASE

Western Wireless Asks FCC to Modernize Its Universal Service Support System

Proposal Would Allow Rural Americans to Benefit from Competitive and Efficient Telecom Services; Consumers Nationwide Could Save Billions in Subsidy Payments

WASHINGTON, D.C. – October 30, 2003 - Western Wireless Corporation (NASDAQ: WWCA) today asked the Federal Communications Commission (FCC) to discontinue using the *Rate-of-Return* (RoR) regulatory system for setting rural telephone companies' universal service support and access charges. Western Wireless argues that RoR bloats the universal service fund, creates opportunities and incentives for waste, fraud and abuse, and inhibits the development of efficient, innovative and competitive services for rural consumers.

"Rate of Return regulation has outlived its time and must be replaced with a more appropriate form of regulation based upon today's competitive environment," said John Stanton, chairman and chief executive officer at Western Wireless Corporation. "This petition will help modernize the federal universal service system, bring the full benefits of the telecommunications revolution to rural Americans and eliminate the ongoing distortions and incentives for over-funding the rural telephone companies that permeate the current system."

Specifically, Western Wireless shows that eliminating RoR regulation would achieve the following benefits:

- **Save Money and Stop Waste, Fraud and Abuse.** By far the largest cause of the growth of the high-cost universal service fund is disbursements to rural telephone companies pursuant to RoR formulas. Independent audits are rarely, if ever, performed on RoR carriers, and in this era of corporate accounting and governance problems, opportunities abound for carriers to overstate or misallocate their costs and thereby increase their access charges and high-cost support. Consumers across the country would save hundreds of millions, possibly billions, of dollars if RoR were eliminated and replaced with a system better targeted to support affordable service for consumers in high-cost areas.

- **Create Incentives for Efficiency.** The FCC has already recognized, as far back as 1988, that RoR regulation gives carriers incentives "to adopt the most costly, rather than the most efficient, investment strategies." In addition, the FCC noted that RoR "may have a negative effect on innovation .... because a carrier's reward for such innovation is a reduction in its dollar earnings." (3 FCC Rcd 3195, 3219-20, 3223) Ending RoR would create incentives for more efficient networks, speed the deployment of new technologies and benefit consumers.

- **Remove Barriers to Competition in Rural Areas.** Rural customers benefit from access to competitive telecommunications alternatives, but RoR regulation is a barrier to full competition. Under RoR regulation, rural telephone companies are able to achieve a guaranteed return on investment on their historical, embedded costs. Unlike the rural telephone companies, competitive carriers receive universal service support only for customers served, which encourage carriers to be efficient and meet the needs of customers.

Western Wireless proposes to replace RoR regulation with a *forward-looking cost-based methodology* based on using the most efficient technology, which would be implemented in 2006 for competitive ETCs, non-rural telephone companies and rural telephone companies owned by relatively large holding companies. These rules would be phased in over the next six years for small rural companies.

"This petition will help the FCC follow through on its pre-existing commitments to rationalize and reconcile the high-cost universal service support system, and to set support based on forward-looking costs. The petition also dovetails well with a number of pertinent and pending FCC proceedings," Stanton said. "The FCC should be congratulated for enacting policies that have encouraged greater investment and deployment in rural America by companies like Western Wireless. By eliminating RoR for universal support, the Commission can take a bold step that will cement the benefits of competition and create strong incentives for both wireless carriers and traditional telephone companies to bring advanced telecommunications services to all rural consumers."

About Western Wireless Corporation

Western Wireless Corporation owns the Cellular One brand and is a leading provider of rural communications to more than a million customers in the Western United States. Based in Bellevue, Wash., the company owns and operates wireless cellular phone systems marketed under the Cellular One national brand name in 19 western states. Cellular One has been one of America's most recognized wireless brands for almost 20 years, since the beginning of cellular telephone service. For more information about Western Wireless, visit www.westernwireless.com. Information on Cellular One may be found at CellularOne.com. Western Wireless is a member of the Cellular Telecommunications and Internet Association (http://www.wow-com.com).

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